# CORONATION BOND FUND

Fund Information as at 31 August 2020

CORONATION

TRUST IS EARNED™

## WHAT IS THE FUND'S OBJECTIVE?

The fund seeks to maximise returns from a diverse range of primarily South African bonds. It aims to outperform the All Bond Index.

## WHAT DOES THE FUND INVEST IN?

The Bond Fund can invest in fixed income instruments, issued by governments, parastatals and private companies, as well as cash. Exposure to foreign assets is limited to 10%. The fund is mandated to make use of derivative instruments for efficient portfolio management purposes.

## IMPORTANT PORTFOLIO CHARACTERISTICS AND RISKS

Risk Profile

5/10
Moderate

Maximum growth/
minimum income exposures

- Growth Assets: 0%
- Income Assets: 100%

The fund is strategically managed to secure an attractive return by investing primarily in a range of government and corporate bonds. It will hold various tactical positions to benefit from the best opportunities as they emerge.

Investments are meticulously researched and subjected to a strict risk management process. Only quality instruments of reputable institutions will be considered. All factors that could affect these investments are carefully monitored, including inflation as well as currency and interest rates.

The risk of losing money over periods of more than a year is low, while it is slightly higher for periods of less than a year. The primary risk exposures are to changes in interest rates and corporate credit events.

## HOW LONG SHOULD INVESTORS REMAIN INVESTED?

The  recommended term is 12 months and longer.

## WHO SHOULD CONSIDER INVESTING IN THE FUND?

Investors who seek the benefits of an actively managed bond fund. The fund is particularly suited to those who require exposure to bonds as part of a diversified portfolio.

## WHAT COSTS CAN I EXPECT TO PAY?

An annual fee of 0.75% (excl. VAT) is payable.

Fund expenses that are incurred in the fund include trading, custody and audit charges. All performance information is disclosed after deducting all fees and other portfolio costs.

We do not charge fees to access or withdraw from the fund.

More detail is available on www.coronation.com

## WHO ARE THE FUND MANAGERS?

NISHAN MAHARAJ
BSc (Hons), MBA

STEVE JANSON
BBusSc

SEAMUS VASEY
BCom (Hons), MSc

## GENERAL FUND INFORMATION

| | |
|---|---|
| Launch Date | 1 August 1997 |
| Fund Class | R |
| Benchmark | BEASSA ALBI Index |
| Fund Category | South African – Interest Bearing – Variable Term |
| Regulation 28 | Does not comply |
| Income Distribution | Semi-annually (March & September) |
| Investment minimum | R5 000 or R500/m debit order |
| Bloomberg Code | CORSPBD |
| ISIN Code | ZAE000019790 |
| JSE Code | CNSB |

# CORONATION BOND FUND

CORONATION
TRUST IS EARNED™

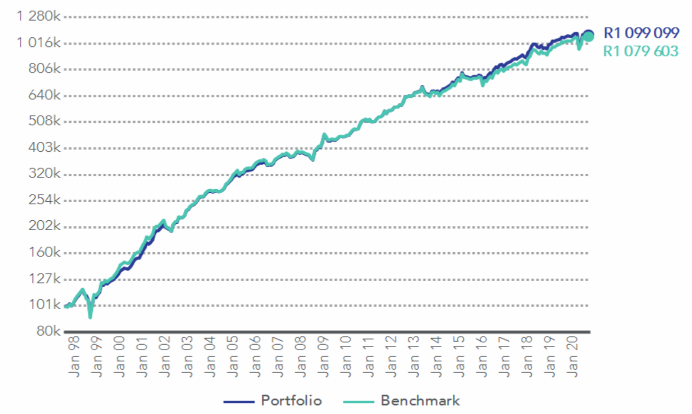
CLASS R as at 31 August 2020

| | |
|---|---|
| Fund category | South African - Interest Bearing - Variable Term |
| Launch date | 01 August 1997 |
| Fund size | R 3.14 billion |
| NAV | 1410.85 cents |
| Benchmark/Performance Fee Hurdle | BEASSA ALBI Index |
| Portfolio manager/s | Nishan Maharaj, Seamus Vasey & Steve Janson |

| | 1 Year | 3 Year |
|---|---|---|
| Total Expense Ratio | 0.87% | 0.87% |
| Fund management fee | 0.74% | 0.74% |
| Fund expenses | 0.02% | 0.02% |
| VAT | 0.11% | 0.11% |
| Transaction costs (inc. VAT) | 0.00% | 0.00% |
| Total Investment Charge | 0.87% | 0.87% |

## PERFORMANCE AND RISK STATISTICS

### GROWTH OF A R100,000 INVESTMENT (AFTER FEES)




### PERFORMANCE FOR VARIOUS PERIODS (AFTER FEES)

| | Fund | Benchmark | Active Return |
|---|---|---|---|
| Since Launch (unannualised) | 999.1% | 979.6% | 19.5% |
| Since Launch (annualised) | 10.9% | 10.9% | 0.1% |
| Latest 20 years (annualised) | 10.4% | 10.0% | 0.4% |
| Latest 15 years (annualised) | 8.3% | 8.0% | 0.3% |
| Latest 10 years (annualised) | 7.9% | 7.7% | 0.2% |
| Latest 5 years (annualised) | 7.6% | 7.6% | 0.1% |
| Latest 3 years (annualised) | 6.6% | 7.7% | (1.2)% |
| Latest 1 year | 1.9% | 4.2% | (2.3)% |
| Year to date | 0.0% | 1.9% | (1.9)% |

| | Fund |
|---|---|
| Modified Duration | 6.4 |
| Yield | 9.2% |

### RISK STATISTICS SINCE LAUNCH

| | Fund | Benchmark |
|---|---|---|
| Annualised Deviation | 7.8% | 8.7% |
| Sharpe Ratio | 0.24 | 0.21 |
| Maximum Gain | 26.3% | 26.4% |
| Maximum Drawdown | (19.0)% | (22.3)% |
| Positive Months | 70.4% | 70.4% |

| | Fund | Date Range |
|---|---|---|
| Highest annual return | 34.9% | Sep 1998 - Aug 1999 |
| Lowest annual return | (7.0%) | Sep 1997 - Aug 1998 |

## PORTFOLIO DETAIL

### ASSET ALLOCATION BY ISSUER TYPE

| | % of Fund |
|---|---|
| Government | 77.0% |
| State Owned Entities | 1.4% |
| Banks and Insurers: NCDs and Deposits | 3.6% |
| Banks: Senior Debt | 10.2% |
| Banks: Subordinate Debt (<12m) | 0.0% |
| Banks: Subordinate Debt (>12m) | 3.6% |
| Insurers | 0.4% |
| Other corporates | 1.9% |
| REITS | 1.8% |
| Total | 100.0% |

### TOP 5 ISSUER EXPOSURE

| | % of Fund |
|---|---|
| Republic of South Africa Government Bonds | 75.6% |
| Nedbank Ltd | 7.3% |
| RMB Holdings | 4.5% |
| Standard Bank of SA Ltd | 2.4% |
| Growthpoint Properties Ltd | 1.8% |

### MATURITY PROFILE DETAIL

| Sector | 31 Aug 2020 |
|---|---|
| 0 to 3 Months | 2.6% |
| 6 to 9 Months | 1.2% |
| 9 to 12 Months | 0.0% |
| 1 to 3 Years | 4.8% |
| 3 to 7 Years | 10.1% |
| 7 to 12 Years | 24.2% |
| Over 12 Years | 57.2% |

### INCOME DISTRIBUTIONS

| Declaration | Payment | Amount | Interest | Dividend |
|---|---|---|---|---|
| 31 Mar 2020 | 01 Apr 2020 | 61.21 | 61.21 | 0.00 |
| 30 Sep 2019 | 01 Oct 2019 | 59.65 | 59.65 | 0.00 |
| 29 Mar 2019 | 01 Apr 2019 | 62.96 | 62.73 | 0.23 |
| 28 Sep 2018 | 01 Oct 2018 | 59.19 | 59.19 | 0.00 |

### MONTHLY PERFORMANCE RETURNS (AFTER FEES)

| | Jan | Feb | Mar | Apr | May | Jun | Jul | Aug | Sep | Oct | Nov | Dec | YTD |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Fund 2020 | 1.19% | (0.09)% | (10.81)% | 3.61% | 7.11% | (1.43)% | 0.29% | 1.09% | | | | | **0.00%** |
| Fund 2019 | 2.73% | (0.33)% | 0.91% | 0.44% | 0.56% | 1.80% | (0.62)% | 0.92% | 0.82% | (0.33)% | (0.27)% | 1.66% | **8.54%** |
| Fund 2018 | 1.87% | 3.93% | 1.79% | (0.31)% | (2.22)% | (0.80)% | 1.92% | (2.54)% | 0.62% | (1.07)% | 3.86% | 0.62% | **7.69%** |

*Issue date: 2020/09/10*

*Please refer to page 4 of the Comprehensive Fact Sheet for important additional infomation, including change in cost disclosures.*

*Please note that the commentary is for the retail class of the Fund.*

We are already six months into 2020, a year that truly defies description, with a landscape that still presents as volatile and treacherous. At the beginning of the year, before the novel coronavirus had turned into a fully-fledged pandemic, it was hard to find a pessimist in financial markets. The subsequent global lockdown sent both the global and local economies into severe recession. Global monetary and fiscal policy then unleashed a flood of money into the economy, the likes of which has never been seen before, spurring expectations for a quick recovery. Asset prices started to recover in the second quarter of the year (Q2-20) as economies across the globe started to open up from 'hard lockdowns'. However, concerns about a second wave of infections in developed markets and escalating infection rates in emerging markets (EMs) threaten to derail the recovery.

## The South African situation

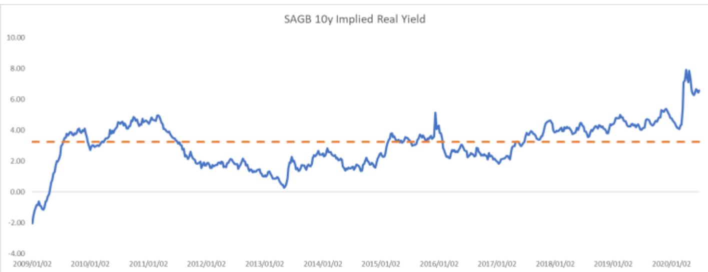
The local economic backdrop is concerning, but valuations were considerably cheaper by the end of the first quarter. South Africa's (SA'S) asset price recovery was buoyed by better risk sentiment in global markets. The All Bond Index (ALBI) was up 9.9% in Q2-20, but its returns remain flat year to date (YTD) and a paltry 2.8% over the last 12 months. ALBI performance continues to be driven by the performance of bonds in the zero- to seven-year area of the curve, as cash rates have pulled down aggressively on the 275 basis points (bps) of repo rate cuts carried out by the South African Reserve Bank (SARB). The 12-year-plus area of the curve has continued to underperform due to the deterioration in government finances and increased public-sector borrowing requirements. Inflation-linked bond (ILB) performance has been dismal, with the Composite Inflation-Linked Index down 3% over the last 12 months, led again by ILBs in the seven-year plus area. Despite poor index performance, ILBs out to seven years have still generated a return more than cash (2.9%) YTD. Overall, bond yields have had a rollercoaster year and are currently only marginally higher than they were during the 'Nenegate' aftermath and considerably lower than during the March sell-off, but still embed a significant risk premium.

EM debt crises have traditionally occurred in countries that predominantly have foreign-denominated debt; face an accelerated decline in their currency, resulting in an increased debt burden that they are unable to service; and an inflationary problem that re-enforces the downward spiral in their currency. SA is slightly different in that inflation will remain modest over the next two to three years. However, due to an incapacitated State, the poor shape of State-owned enterprises, a lack of targeted structural reform and a dearth of political direction, government finances have deteriorated to such an extent that debt service costs are the fastest-rising government expenditure item. In the fiscal year 2020/21, the fiscal deficit will register a whopping -15%, the debt-to-GDP ratio will exceed 80%, tax revenue will be down R300 billion and nominal growth will be down 3.5%. Many countries around the world, both developed and emerging, will face a similar reality as the fiscal taps open to soften the fallout from the Covid-19 pandemic. Unfortunately, due to its poor starting position, glacial pace of reform implementation and reliance on foreign portfolio flows, SA is teetering on the edge of a debt trap.

Local public sector borrowing requirements will push up to almost R800 billion this year, due to the drop-off in tax revenue. Over the longer term, more steps are needed to ensure that the underlying growth engine is restarted through targeted, efficient and transparent investment into the local economy by government and the private sector. In the interim, SA will have to rely on funding from international finance institutions (IFIs) such as the International Monetary Fund and the World Bank, as well as capital markets, to keep the ship afloat. IFI funding is relatively cheap and has little conditionality, but will still need to be repaid in foreign currency, while local capital market funding will have to be accompanied by a strong commitment to reel in wasteful expenditure, refocus current expenditure and implement key sector reforms (e.g. energy, labour and transport) in order to increase investor confidence and trust. SA has a long history of not delivering on key policies and reforms, which has resulted in the current debt nexus and erosion of investor confidence in the country.

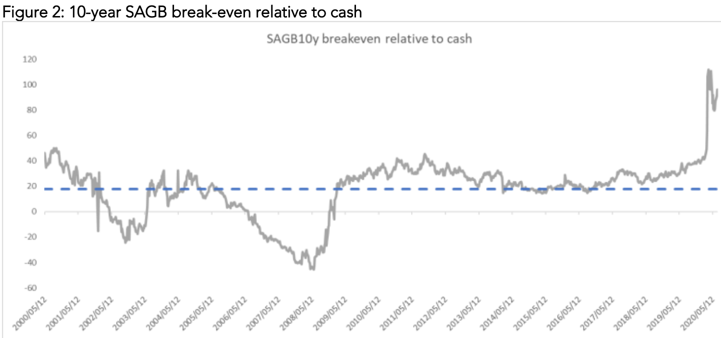
Consumer price inflation will average 2.7% over the next year and 3.5% over the next two years. Following the cumulative 275bps rate cuts since the beginning of this year, the SARB has room to reduce rates by another 50bps over the next three to six months and is likely to keep them at similar levels over the next 12 to 18 months to support the economic recovery. The 10-year South African Government Bond (SAGB) currently trades at 9.5%, which implies a real yield (return after inflation) of 6.6% and a break-even to cash (the extent to which bond yield can widen before its return equals cash) of 93bps over the next year. In figures 1 and 2, one can clearly see that both the implied real yield and break-even relative to expected cash remain at very extended levels relative to history and to their long-term average. This suggests that, from a local perspective, there is a significant risk premium in place due to the poor fiscal outlook.

Figure 1: 10-year South African Government Bond implied real yield




Sources: Bloomberg; Coronation

Figure 2: 10-year SAGB break-even relative to cash




Sources: Bloomberg; Coronation

## The global outlook

Globally, bond yields and policy rates are testing their zero bounds. US 10-year yields, which are widely accepted as the proxy for global bond yields, are trading at historic lows. The Federal Reserve Board (the Fed) has injected massive amounts of stimulus through its open-ended quantitative easing programme, and policy rates and bond yields are not expected to move materially away from their current levels at any time soon. Even if bond yields do push higher due to structural changes in employment and inflation, fair value is not materially more than 1.5% on the US 10-year bond. SA 10-year bonds trade at a spread of 9% above US 10-year bonds, which, once again, is considerably above historic levels and the long-term average. If US bonds were to gravitate towards the 1.5% level, unless this is accompanied by a massive inflation shock, the SA spread over US bonds does have a significant cushion to absorb this move, and would still trade at a historically wide spread. Add to this the fact that the 10-year SAGB trades at a significantly wider real yield than its EM peer group, and one can see that, even from a global perspective, a significant risk premium remains in place.

## A volatile curve

The yield curve has been as volatile (if not more volatile) as outright bond yields. SA now has the steepest yield curve in the tradeable EM universe. The 10-year bond trades 1.7% above the 6.5-year bond, the 15-year bond trades 1.5% above the 10-year bond and the 20-year bond trades 2% above the 10-year bond. Due to the higher yields on offer in the 10-year-plus area of the curve, the inherent break-even protection in these yields, both relative to cash and inflation, is attractive. Our base-case assumption is that the repo rate settles at 3.25% over the next six months and stays there for at least the next 12 months. This implies a cash average of 3.35% over the next 12 months. If we assume inflation comes through more strongly and base rates rise more aggressively to average 4% over the next year, this implies a peak repo rate of close to 5% at the end of year one (250bps of hikes). We use similar assumptions over two and three years, and then run a total return analysis to understand how much the various bonds can sell off before their returns equal cash, as illustrated in Table 1. As can be deduced from the table, the 15-year area of the curve offers the most protection. Combine this with the fact that the 15-year point is steeper than it has ever been relative to the 10-year area (1.5% above), the five-year area (4.4% above) and cash (7.3% above), and its appeal increases. In addition, at the special adjustment Budget in June, Finance Minister Tito Mboweni reinforced the point that National Treasury plans to shorten the duration of its issuance profile to seven to 10 years, suggesting less issuance and, hence, less supply pressure in the >10-year area of the curve. The intentions set out in the June budget are ambitious, and the lack of the flattening of the yield curve bears testament to that. However, if the Treasury were able to get just half of its intentions through, the result would still be more positive than current market pricing, and the yield curve should enjoy significant flattening. The current valuation of the 15-year point is quite attractive due to its inherent break-even protection relative to cash and inflation, as well as the negativity priced into its elevated spread relative to shorter-dated bonds. We therefore view it as an attractive relative allocation on the local bond curve.

Table 1: Average break-even rates

| Bond | Maturity | Yield | 1y B/E (Cash @ 4%) | 2y B/E (Cash @ 5.25%) | 3y B/E (Cash @ 6.25%) |
|---|---|---|---|---|---|
| R186 | 21-Dec-26 | 7.71% | 0.92% | 1.50% | 1.70% |
| R2030 | 31-Jan-30 | 9.41% | 0.94% | 1.65% | 2.15% |
| R2032 | 31-Mar-32 | 10.33% | 0.99% | 1.77% | 2.38% |
| R2035 | 28-Feb-35 | 10.99% | 1.01% | 1.83% | 2.49% |
| R2040 | 31-Jan-40 | 11.44% | 1.00% | 1.81% | 2.47% |
| R2044 | 31-Jan-44 | 11.56% | 0.98% | 1.78% | 2.43% |
| **Average Break-Even** | | | 0.97% | 1.72% | 2.27% |

Sources: Bloomberg; Coronation

The fallout from the Covid-19 pandemic will linger for some time to come. In SA, the impact will be felt most in a much dimmer growth outlook, which will have a severe impact on government finances. The effects of the very hard lockdown and poor policy choices will weigh heavily on the economy going forward. As the economy was not well positioned going into the crisis, strong reforms are needed to return the country to a structurally better growth path, although lower interest rates will lend support to the economy through this difficult phase. SAGBs do embed a decent risk premium, although this premium has reduced slightly post the recovery in Q2-20. As mentioned, SA is on the brink of a debt trap and, although promises have been made to restore the country to a more sustainable debt trajectory, the implementation risks remain elevated. The valuation of SAGBs does provide some offset to this, implying that local bonds do warrant at least a neutral allocation in portfolios.

Portfolio managers
Nishan Maharaj, Steve Janson and Seamus Vasey
as at 30 June 2020

## IMPORTANT INFORMATION THAT SHOULD BE CONSIDERED BEFORE INVESTING IN THE CORONATION BOND FUND

Unit trusts should be considered medium- to long-term investments. The value of units may go down as well as up, and therefore Coronation does not make any guarantees with respect to the protection of capital or returns. Past performance is not necessarily an indication of future performance. The fund is mandated to invest up to 10% of its portfolio into foreign securities and may as a result be exposed to macroeconomic, settlement, political, tax, reporting or illiquidity risk factors that may be different to similar investments in the South African markets. Fluctuations or movements in exchange rates may cause the value of underlying investments to go up or down. The asset allocation by issuer type and top 5 issuer exposures are not reflected on a look-through basis. Coronation Management Company (RF) (Pty) Ltd is a Collective Investment Schemes Manager approved by the Financial Sector Conduct Authority in terms of the Collective Investment Schemes Control Act. Portfolio managed by Coronation Asset Management (Pty) (FSP 548) Ltd, an authorised financial services provider. The Management Company reserves the right to close the fund to new investors if we deem it necessary to limit further inflows in order for it to be managed in accordance with its mandate. Unit trusts are allowed to engage in scrip lending and borrowing. Standard Chartered has been appointed as trustees for the fund (www.sc.com/za; 011-2176600). Coronation is a full member of the Association for Savings & Investment SA (ASISA).

## HOW ARE UNITS PRICED AND AT WHICH PRICE WILL MY TRANSACTION BE EXECUTED?

Unit trusts are traded at ruling prices set on every trading day. Fund valuations take place at approximately 15h00 each business day, except at month end when the valuation is performed at approximately 17h00 (JSE market close) and forward pricing is used. Instructions must reach the Management Company before 14h00 (12h00 for the Money Market Fund) to ensure same day value. The payment of withdrawals may be delayed in extraordinary circumstances, when the manager with the consent of the fund trustees deem this to be in the interest of all fund investors. These circumstances may include periods when significant underlying markets suspend trading which will prevent accurate valuation of the instruments held in the fund. When the suspension of trading relates to only certain assets held by the fund, these assets may be side-pocketed. This process allows normal liquidity on the assets that can be valued, but will delay liquidity on the affected portion of the fund. If the fund is faced with excessive withdrawals, the affected withdrawals may be ring-fenced, which is the separation and delayed sale of the assets reflecting the interest of the liquidity seeking investors. It ensures that the sale of a large number of units will not force Coronation to sell the underlying investments in a manner that may have a negative impact on remaining investors of the fund.

## HOW WAS THE PERFORMANCE INFORMATION INCLUDED IN THIS FACT SHEET CALCULATED?

Performance is calculated by Coronation as at the last day of the month for a lump sum investment using Class R NAV prices with income distributions reinvested. All underlying price and distribution data is sourced from Morningstar. Performance figures are quoted after the deduction of all costs (including manager fees and trading costs) incurred within the fund. Note that individual investor performance may differ as a result of the actual investment date, the date of reinvestment of distributions and dividend withholding tax, where applicable. Annualised performance figures represent the geometric average return earned by the fund over the given time period. Unannualised performance represents the total return earned by the fund over the given time period, expressed as a percentage. Growth charts are shown in logarithmic scale (base 2).

## WHAT IS THE TOTAL EXPENSE RATIO (TER) AND TRANSACTION COSTS (TC)?

TER is calculated as a percentage of the average net asset value of the portfolio incurred as charges, levies and fees in the management of the portfolio. The TER charged by any underlying fund held as part of a fund's portfolio is included in the fund expenses portion of the TER, but trading and implementation costs incurred in managing the fund are excluded. A higher TER does not necessarily imply a poor return, nor does a low TER imply a good return. The current TER may not necessarily be an accurate indication of future TER's. The 1 year TER is for the 12 months to end of September 2019 (updated annually). The 3 year TER is for a rolling 36-month period to the last quarter end (December, March, June and September).

Transaction costs are a necessary cost in managing a fund and impacts the fund's return. They should not be considered in isolation as returns may be impacted by many other factors over time including market returns, the type of fund, the investment decisions of the investment manager and the TER.

The Total Investment Charge is the sum of the Total Expense Ratio (TER) and transaction costs.

## ADVICE AND PLATFORM COSTS

Coronation does not provide financial advice. If you appoint an adviser, advice fees are contracted directly between you and the adviser. For more information please contact the relevant platform (Linked Investment Service Provider or Life Assurance Provider).

## WHERE CAN I FIND ADDITIONAL INFORMATION?

Additional information such as daily fund prices, brochures, application forms and a schedule of fund fees and charges is available on our website, www.coronation.com

## IMPORTANT INFORMATION REGARDING TERMS OF USE

This document is for information purposes only and does not constitute or form part of any offer to issue or sell, or any solicitation of any offer to subscribe for or purchase any particular investment. Opinions expressed in this document may be changed without notice at any time after publication. We therefore disclaim any liability for any loss, liability, damage (whether direct or consequential) or expense of any nature whatsoever which may be suffered as a result of or which may be attributable, directly or indirectly, to the use of or reliance upon the information.